SENATE RECORD VOTE ANALYSIS

104th Congress — June 28, 1995, 10:45 a.m.
1st Session — **Vote No. 295** — Page S-9219 Temp. Record

PRIVATE SECURITIES LITIGATION/Final Passage

SUBJECT: **Private Securities Litigation Reform Act of 1995 . . . H.R. 1058. Final passage, as amended.**

ACTION: BILL PASSED, 69-30

SYNOPSIS: As amended and passed, H.R. 1058, the Private Securities Litigation Reform Act, will enact changes to current private securities litigation practices in order to discourage unjust suits and to provide better information and protection from fraud for investors. Details are as follows:

- brokers or dealers will be prohibited from soliciting or receiving any type of fee or remuneration for helping an attorney in obtaining representation of a customer in private actions;
- a court will determine if attorneys may be barred from representing a client in a securities lawsuit if their ownership of stock subject to that suit creates a conflict of interest of if another conflict of interest exists that is sufficient to justify barring their representation;
- it will generally be prohibited to pay attorney's fees from disgorgement funds;
- each plaintiff who seeks to serve as a representative in a class action lawsuit will have to present a sworn certification of several factors, including that he or she was not hired by a lawyer to file suit and that he or she will not receive a bonus for serving as a class representative;
- a class representative's recovery in a suit will be limited to his or her pro rata share of the settlement or final judgment;
- the filing of settlements under seal will be prohibited unless "good cause" is shown;
- attorney fees awarded by a court to counsel for a plaintiff will be limited to a "reasonable" percentage of the amount of recovery for the class;
- for any proposed or final settlement agreement to a class action lawsuit, the class will have to be informed: of the amounts of damages that the settling parties believe will be collected, on a per-share basis (if there is disagreement each party will have to state the amount it believes will be collected); any intention to use part of the award to pay legal fees; the reason for any proposed settlement; and other specified information;

(See other side)

YEAS (69)			NAYS (30)		NOT VOTING (0)	
Republicans (49 or 92%)		Democrats (20 or 43%)	Republicans (4 or 8%)	Democrats (26 or 57%)	Republicans (0)	Democrats (0)
Abraham	Helms	Baucus	Cohen	Akaka		
Ashcroft	Hutchison	Bradley	McCain	Biden		
Bennett	Inhofe	Dodd	Shelby	Bingaman		
Brown	Jeffords	Exon	Specter	Boxer		
Burns	Kassebaum	Feinstein		Breaux		
Campbell	Kempthorne	Ford		Bryan		
Chafee	Kyl	Harkin		Bumpers		
Coats	Lott	Johnston		Byrd		
Cochran	Lugar	Kennedy		Conrad		
Coverdell	Mack	Kerry		Daschle		
Craig	McConnell	Kohl		Dorgan		
D'Amato	Murkowski	Lieberman		Feingold		
DeWine	Nickles	Mikulski		Glenn		
Dole	Packwood	Moseley-Braun		Graham		
Domenici	Pressler	Murray		Heflin		
Faircloth	Roth	Nunn		Hollings		
Frist	Santorum	Pell		Inouye		
Gorton	Simpson	Reid		Kerrey		
Gramm	Smith	Robb		Lautenberg		
Grams	Snowe	Rockefeller		Leahy		
Grassley	Stevens			Levin		
Gregg	Thomas			Moynihan		
Hatch	Thompson			Pryor		
Hatfield	Thurmond			Sarbanes		
	Warner			Simon		
				Wellston		

VOTING PRESENT(1)
Bond

EXPLANATION OF ABSENCE:
1—Official Buisiness
2—Necessarily Absent
3—Illness
4—Other

SYMBOLS:
AY—Announced Yea
AN—Announced Nay
PY—Paired Yea
PN—Paired Nay

- after a complaint is filed, it will be published so that members of the purported class may learn of the complaint and, within 60 days, apply to be lead plaintiff;
- a rebuttable presumption will be established that the plaintiff with the largest financial stake in an action should be named lead plaintiff (see vote No. 287 for related debate);
- the lead plaintiff will select the lead counsel;
- upon final adjudication of a private securities action, a judge will review the record for compliance with rule 11 of the Federal Rules of Civil Procedure (which bars frivolous, harassing, and other legal maneuvers), and will require any party guilty of rule 11 violations to pay the other parties' legal fees, with exceptions (see vote No. 291 for related debate):
- discovery will generally be stayed upon a motion to dismiss (see vote No. 292 for related debate);
- plaintiffs alleging untrue statements of material facts, or the omission of material facts necessary to keep statements from being misleading, must specify the statements and omissions forming the basis of their allegations, and why they believe their allegations are true;
- to recover damages based on the defendant's state of mind, a plaintiff must specifically allege facts giving strong inference that the defendant acted with the required state of mind, which may be shown using specified evidentiary standards (see vote No. 293);
- a safe harbor from securities litigation will be created for forward-looking statements, whether written or oral, that clearly and proximately note that they are projections, and that actual results may differ materially; no safe harbor will be created for forward-looking statements made with the purpose and actual intent of misleading investors; numerous other exemptions from the safe-harbor, mostly for certain types of businesses, are also listed (for related debate, see vote Nos. 288-289 and 294);
- victims of fraudulent forward-looking statements will be eligible for funds from disgorgement actions by the Securities and Exchange Commission (SEC);
- in private actions, defendants will have the right to a written interrogatory for each allegation based on their state of mind;
- application of the Racketeer Influenced and Corrupt Organizations (RICO) Act to securities suits will be limited;
- the SEC will be given statutory authority to prosecute knowing aiders and abettors of securities fraud (see vote No. 286 for related debate);
- a defendant will not have to pay damages to a plaintiff for losses unrelated to misstatements or omissions which caused a securities loss;
- a study will be done of the protection senior citizens are afforded by this Act from securities fraud (see vote No. 285);
- a plaintiff's damages will not exceed the difference between the purchase or sale price, as appropriate, by the plaintiff for the security and the median market price in the 90 days after the defendant corrects the misstatements or omissions;
- joint and several liability will be retained for defendants who commit "knowing" securities fraud, but a modified proportionate liability standard will be applied to defendants who are found guilty of "reckless" conduct (see vote No. 284 for related debate); and
- independent public accountants will be required to first notify a company's management of any illegal activity they discover, and, if the management fails to act, they will be required to notify the company's board of directors, and if the board of directors fails to notify the SEC within 1 day, they must notify the SEC the following day.

NOTE: Immediately prior to final passage, the Senate struck all after the enacting clause and inserted in lieu thereof the text of S. 240, as amended.

Those favoring final passage contended:

This bill is good for America and bad for the approximately 90 lawyers who are guilty of filing frivolous securities litigation suits. Twenty or thirty years ago these few unethical lawyers would have been disbarred for committing champerty, which is the pursuit of litigation by lawyers that is more beneficial to them then their clients. The judges of yesteryear would not have toleratedlawyers advertising nationwide for clients and then keeping an average 86 cents on the dollar for themselves and their investigators. Today, though, judges accept a body of case law that has slowly developed that permits disreputable, sleazy lawyers to extort money for themselves from innocent corporations by making baseless allegations of fraud. As one of these buccaneer barristers recently crowed in *Forbes* magazine, "I have the greatest practice in the world. I have no clients."

The common practice of this small number of lawyers is to file class action suits alleging hundreds of millions of dollars of fraud. The suits name defendants according to their wealth; any company with money, no matter how peripherally related to a suit, is named. In 93 percent of the cases, companies then settle for a few million dollar payment, with most of the money going to the lawyers, and a small sum going to the class the lawyers pretended to represent. Usually, the lead plaintiff will be a small investor who is paid by lawyers for the right to file a class action suit on his or her behalf. That small investor usually gets a bonus from the lawyers. If companies do not settle, they must spend millions of dollars in defending themselves. Most of those costs are due to discovery, which requires them to turn over reams of documentation to any lawyer who accuses them of fraud. The lawyers then pick through the documents hoping to find some little detail they can distort before a jury. Juries, for their part, will almost always rule against the plaintiffs. However, even the most frivolous suits sometimes succeed, because juries will misapply the law, especially in complex areas such as securities litigation. Juries are especially prone to misapply the law in securities cases because the law has never actually been written--it exists almost entirely as a court-created right, that varies from jurisdiction to jurisdiction and that even varies from case to case within a jurisdiction. A company that is threatened with a several hundred million dollar lawsuit, no matter how baseless, will not usually fight it and risk the 5 percent to 10 percent chance that it will lose and be bankrupted.

The purpose of our securities laws is to provide investors with timely and accurate information on public companies so that they may make informed decisions on their securities transactions. Clearly the current system is not working. A few lawyers make millions on frivolous suits, growing companies are unwilling to provide information on their operations for fear of being sued, large companies refuse to associate with smaller companies for fear of being named as partners in unjust suits, and even in legitimate suits lawyers rip-off their clients by settling quickly for millions of dollars for themselves and only pennies on the dollar for the real losses suffered by their clients. Investors are severely hurt because they do not get timely and accurate information, plus, when they are victims of fraud, they are not compensated.

This bill will totally reform the current system. Starting from the filing of a suit, several measures will be enacted that will make sure that the suit is not frivolous. Those measures include that it will be illegal for brokers to provide lists of investors to lawyers or to pay a pet lead plaintiff a bonus to represent it. Further, every class action suit will be advertised so that class members will have a chance to join, and a rebuttable presumption will exist that the plaintiff with the greatest financial interest (generally an institutional investor representing tens of thousands of clients) should be the lead plaintiff. Next, the bill will take steps to make sure that only those who are guilty of fraud are pursued in securities cases. Those steps include a codification of the Supreme Court ruling that no private right of action exists for alleging aiding and abetting (this weak standard has been heavily abused by lawyers to sue large companies that have tenuous connections with smaller companies that they have accused of committing fraud), and a safe harbor will be created for forward-looking statements. Finally, when a suit is settled, the reforms that will be made by this bill include that the liability of defendants who are only peripherally involved will be limited, that lawyers will have to disclose their settlements, that attorneys' fees will be limited, and that any judgment will be fairly distributed among the plaintiffs on a pro rata basis.

The reforms in this bill are strongly supported by both investors and businesses. Many investors even view this bill as too modest. In fact, we do not know of any opposition that does not come from lawyers, newspaper editorialists, and government regulators. The last group is certainly not united in opposition; we have endorsements from the pension fund administrators and regulators of many States.

In addition to the usual suspects (lawyers, pundits, and bureaucrats) who are opposed to this bill, our colleagues also claim that we should list the elderly. They are wrong. In March, 1995, the National Investor Relations Institute commissioned a poll of Americans age 50 and over who invest in either stocks or mutual funds. That poll found the following: 87 percent think that securities lawsuits divert scarce funds that can be used on product research and business expansion; 79 percent believe that defendants should only pay damages according to their percentage of fault; and 81 percent favor making a lawyer who files a frivolous suit pay the legal fees of both sides. Seventy percent of the poll respondents also said at least one member of their household was a member of AARP, which opposes this bill. Our colleagues' only evidence for saying that senior citizens oppose this bill is that AARP opposes it; we suggest that they should worry more about what senior citizens themselves want instead of what a special interest group that is clearly out of touch with its membership says they want.

All of the major investment organizations, 10 of the biggest public pension funds, 12 State pension fund administrators and regulators, and hundreds of companies have all expressed support for this bill. Both plaintiffs and defendants want Senators to pass H.R. 1058. We will not disappoint them.

Those opposing final passage contended:

From the beginning of the debate on this bill we have been willing to concede that some frivolous securities suits are filed, and we have concurred that steps should be taken to stop those suits. However, this bill will do far more than block frivolous suits; it will make it so difficult to sue for legitimate reasons that it will virtually give unscrupulous individuals a license to steal. This is a Trojan Horse bill; on the outside, its stated purpose is reasonable, but its inner details are full of nasty surprises.

For the last 6 decades the United States has enjoyed the world's safest securities markets. These markets have not been crippled by a litigation explosion; in the past 20 years, the amount of capital they attract has increased tremendously, while the number of suits filed has remained steady at about 300 per year. To further illustrate how minor the problem is, we inform our colleagues that there are some 14,000 companies that have filings with the SEC, but each year only about 140 out of those 14,000 are brought in as party defendants in class action suits.

To eliminate the few cases out of the 300 or so that are filed each year that are frivolous, this bill will so limit the right to file suit that it will not only discourage frivolous suits, it will also make it nearly impossible to win legitimate suits. The bill will fail to overturn the 1-year/3-year statute of limitations that the Supreme Court unwisely set last year as the national standard; it will surrender control of class action suits to the wealthiest member of the class (who frequently is a party to the fraud that is the subject of the suit); it will create a safe harbor for forward-looking statements that will protect deliberate lies; it will eliminate the right of private parties to sue aiders and abettors; it will limit RICO liability; and it will overturn hundreds of years of tort law precedence by sharply limiting the doctrine of joint and several liability for damages. These and other changes will create a simple, "buyer beware" investment system that will lead to massive fraud. Human nature being what it is, if people know they can legally get away with defrauding investors, they will. Just as deregulation of the thrift industry contributed to its massive failure, we fear that this bill will cause such widespread fraud that a several hundred billion dollar bailout will be needed in a few years.

We should not go through such an exercise. The current system needs only a few minor tweaks to get rid of frivolous suits; the right of defrauded investors to sue does not need to be discarded. Fifty major newspapers, literally every legal group involved in securities fraud litigation (both public and private) and senior citizens are solidly opposed to this bill, and for good reason: it will promote fraud. Unfortunately, though, the die is cast; we will vote against this bill, but we know a majority of Senators will vote in its favor. If H.R. 1058 becomes law, we are certain they will live to regret their votes.